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STAFF REPORT

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ORIGINAL

CHIEF CLERK'S OFFICE

SUBJECT:

Recommendation to enter an order directing MANK, LTD to show cause why the Commission's Order in Docket No. 95-0236 should not be vacated.

SUMMARY:

In Docket No. 95-0236, the Commission approved MANK, LTD ("MANK") as a Qualified Solid Waste to Energy Facility¹ ("QSWEF") for 3 MW of generation at the CDT landfill site, Joliet, Illinois. (Order p. 2, February 22, 1996) However, from information available to Staff, it appears that MANK never developed a QSWEF on the site. MANK is no longer the owner of the landfill gas to energy facility approved in Docket No. 95-0236. In fact, MANK has attempted to improperly transfer ownership of the facility to another corporate entity, i.e., has purported to transfer ownership without Commission approval.

Section 8-403.1(b) of the Illinois Public Utilities Act ("the PUA" or "the Act") states that:

(b) For the purpose of this Section and Section 9-215.1, "qualified solid waste energy facility" means a facility determined by the Illinois Commerce Commission to qualify as such under the Local Solid Waste Disposal Act, to use methane gas generated from landfills as its primary fuel, and to possess characteristics that would enable it to qualify as a cogeneration or small power production facility under federal law.

Thus, the Act requires that the Commission determine whether a specific facility meets the requirements to be a QSWEF. In addition, the Commission must determine whether the owner of each proposed facility qualifies for a retail rate contract.

Section 8-403.1(e) of the Illinois Public Utilities Act ("the PUA" or "the Act") addresses the ownership criteria for QSWEFs and states that:

(e) The Illinois Commerce Commission shall not require an electric utility to purchase electricity from any qualified solid waste energy facility which is owned or operated by an entity that is primarily engaged in the business of producing or selling electricity, gas, or useful thermal energy from a source other than one or more qualified solid waste energy facilities.

Any and all owners must be found by the Commission to meet the criteria in subsection (e) before they can obtain a contract to sell electricity to a utility. If the ownership criteria of the law are not met, then there is no entitlement to a contract for the Retail Rate. Thus,

¹ Commission approval of a QSWEF is pursuant to Section 8-403.1 of the Public utilities Act (PUA), and is administered through the Commission's rules 83 Ill. Adm. Code 445.

whenever a landfill gas facility changes ownership, the new owner must gain Commission approval under provisions of Section 8-403.1(e) of the Act. Without that approval from the Commission, an electric utility is not required to enter into a contract to pay the retail rate for the electricity generated by the landfill gas facility. If the facilities are sold or transferred by the approved owner of the QSWEF to another entity, the purchasing entity must be separately approved by the Commission in order to assume the ongoing retail rate contract. The original QSWEF owner can no longer qualify for the benefit of a retail rate contract because it no longer possesses the facilities for which the Commission's original determination was applicable. Concomitantly, without that approval and the resulting Retail Rate contract, a utility would not be entitled to tax credits for the difference between the retail rate and its avoided cost for power.

There is no question that Commission approval is required for not only the initial petitioning owner, but also for each subsequent owner; Commission approval of an owner is not transferable. The reason for this is to prevent an owner that would not qualify for a Retail Rate contract under Section 8-403.1 (e) from engaging in an end-run around the statute's clear limitations by obtaining a qualified facility from a qualified owner.

In the case of MANK, it appears that MANK, the approved owner, never built or operated a generation facility. Rather, MANK purported to transfer its approval to own and operate a QSWEF to another entity. Staff believes that vacating the MANK Order is warranted because of the transfer of ownership of the facilities to an entity not found to be qualified by the Commission, and to discourage entities from gaming the ownership requirements of the Act. Thus, it is Staff's recommendation that the Commission enter an Order that directs MANK to show cause why the Order in Docket No. 95-0236 should not be vacated.

BACKGROUND:

Shortly after MANK received QSWEF approval from the Commission, MANK was acquired by KMS Joliet Power Partners, L.P. ("KMS Joliet") possibly in June of 1997.² KMS Joliet has not petitioned the Commission for approval as a QSWEF. KMS Joliet notified the Chief Clerk on January 2, 1997, well after the MANK proceeding in Docket No. 95-0236 was closed, that it acquired and was the operator of MANK. Despite the fact that KMS Joliet received a date stamped copy of their letter from the Chief Clerk, KMS Joliet is not an approved QSWEF because notification of the Chief Clerk does not constitute approval by the Commission. Sections 8-403.1(b) & (e) of the Act require that the Commission approve the acquisition of MANK by KMS Joliet.

KMS Joliet is 100% owned by KMS Power Income Fund ("KMS PIF"). It is Staff's understanding that KMS PIF is an investment fund that owns several power generating facilities in the United States and Canada, and is traded on the Toronto Stock Exchange. Following KMS Joliet's acquisition of MANK, KMS PIF was acquired in the fourth quarter of 2001 by the Algonquin Power Income Fund ("Algonquin PIF").³ Algonquin PIF is an open-ended investment trust, established under the laws of Ontario, Canada, that owns

² According to the most recently available annual report of KMS PIF, KMS Joliet was acquired by KMS PIF on June 10, 1997.

³ AG PIF Annual Report 2001, p.1.

numerous power generating facilities in the United States and Canada.⁴ These changes of ownership are established by documents provided by representatives of KMS Joliet and other publicly available information, such as annual reports of KMS PIF and Algonquin PIF, and confirm that these entities have acquired the landfill gas to energy facilities located at the CDT landfill in Joliet. Both KMS PIF and Algonquin PIF appear to hold more non-QSWEF generation than QSWEF generation. Thus, if the various corporate reports are accurate, then both KMS PIF and Algonquin PIF are "primarily engaged" in generation from sources other than QSWEFs, and thus, neither could have qualified for a contract pursuant to Section 8-403.1(e). See ICC Staff Report Attachment 1 for a flow chart that sets forth Staff's understanding of MANK and the various KMS companies.

Staff is not certain about the timing of the following sequence of events, but it appears that MANK was divided into two separate facilities, one facility owned by KMS Joliet and the other MANK facility owned by KMS Joliet II Power Partners, L.P. ("KMS Joliet II"). This was done without Commission review or approval. KMS Joliet II is 100% owned by KMS Energy, Inc. ("KMS Energy"), which is part of a chain of subsidiary companies, whose parent, KMS International, owns two other Commission approved QSWEFs. In Docket No. 98-0670, KMS International is identified as the parent/owner of KMS Morris Power, Inc. ("KMS Morris") and KMS Energy. (Order p. 1, 12/08/1999) Since KMS International owns 100% of KMS Energy, then it also owns 100% of KMS Macon Power, Inc. ("KMS Macon"), which received Commission approval as a QSWEF in Docket No. 98-0163. In short, KMS International owns KMS Energy, KMS Morris, KMS Macon, and KMS Joliet II.

It is clear, due to the ownership change, that MANK does not own the Commission approved facilities to produce power from landfill gas at the CDT landfill in Joliet, and MANK does not receive a retail rate payment from ComEd for the power produced from the CDT landfill at Joliet.

As further evidence that KMS Joliet and KMS Joliet II are the owners of the landfill gas to energy facilities at the CDT landfill in Joliet, Staff cites a correspondence between KMS Joliet, KMS Joliet II, and ComEd that is included as ICC Staff Report Attachment 2. In that correspondence, the two owners of the separate facilities at the CDT Landfill in Joliet formally request that ComEd begin splitting the payments according to meter number. Specifically, the letter states in part:

*It is important that you understand that **KMS Joliet and KMS America** are no longer related in anyway to **KMS Joliet II and KMS Energy Inc.** However, the payment made by ComEd for electricity purchased from **the two projects** is issued as one payment and deposited to one bank account.
Please accept this letter as **a formal request by both owners** to have ComEd correct this situation and pay the appropriate party their respective amount directly. (emphasis added)*

Clearly, the letter indicates that there are two owners of two "projects" at the CDT landfill in Joliet and neither owner is MANK.

⁴ AG PIF Annual Report 2001, p.1.

MANK has been able, at any time, to seek approval from the Commission for any additional facilities that it owns or has installed at the CDT landfill in Joliet, subsequent to their original Commission Order, but it has not. KMS Joliet and KMS Joliet II have been able, at any time since acquiring the MANK facilities, to file a petition with the Commission to be approved as QSWEF owners, but they have not. Meeting the ownership criteria of section 8-403.1(e) is normally not difficult. For example, if KMS Joliet and KMS Joliet II could show that neither they nor any of their affiliates have more than a fifty percent (50%) ownership interest in any electric generating facilities, other than those that have been determined by the Commission to be QSWEFs, then KMS Joliet and KMS Joliet II could comply with section 8-403.1(e) of the Act. However, it appears that both of KMS Joliet and KMS Joliet II's owners own several non-QSWEF power generating facilities: those facts may explain why KMS Joliet and KMS Joliet II did not, of their own accord, petition the Commission for approval as a QSWEF.

Based on information set forth on the Internet site of KMS Energy, there appears to be a working relationship between KMS Energy and KMS PIF such that Staff questions whether KMS Energy would comply with section 8-403.1(e) of the Act. It appears that KMS Energy has ownership and/or operating interests in several non-QSWEF power generating facilities. Staff recommends that the Commission take action to vacate the MANK Order to discourage what may be attempts to circumvent the law's requirements. The Commission's interpretation and application of the Retail Rate Law has included the limitation of approving only one QSWEF at each landfill site. Thus, in past instances where a new petitioner wished to construct and operate a landfill-methane based generator at a landfill site where a QSWEF approval exists for another owner, the Commission has required the previously approved QSWEF owner to actively and formally relinquish its QSWEF status on the record.


In addition, the Commission should vacate the MANK Order because such action is consistent with and promotes the law's intent, as set forth in Sec. 8-403.1(a) of the Act:

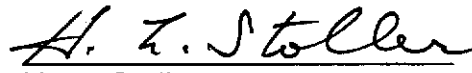
- (a) It is hereby declared to be the policy of this State to encourage the development of alternate energy production facilities in order to conserve our energy resources and to provide for their most efficient use.

Since MANK no longer owns the facilities that were approved by the Commission in Docket No. 95-0326, MANK can no longer promote the intent of the law because it cannot produce electricity from the alternate energy resources at the CDT landfill in Joliet. Moreover, because the Commission must approve both the facilities and the ownership of the facilities for QSWEF status, MANK's approval must be rescinded by the Commission, by vacating the Order, so that any other entity may properly apply for and gain approval by the Commission as a QSWEF. In short, the Order in Docket No. 95-0236 must be vacated by the Commission to ensure that another entity can qualify as the owner of the facilities at the CDT landfill at Joliet. The intent of the Act that electricity be produced from landfills will be thwarted until the Commission acts to vacate the MANK Order.

It appears that State tax credits for purchases of QSWEF-generated power have been taken by ComEd for some time for the CDT landfill at Joliet. At the conclusion of any enforcement proceeding initiated by the Commission as a result of this Staff Report, if the Commission determines that its MANK order should be vacated, the Department of Revenue should be notified of these circumstances, so that it can determine the proper course of action regarding the prior tax credits that were issued in association with the electricity purchased from the CDT landfill facilities at Joliet. In the interim, Staff will notify the Department of Revenue of the circumstances surrounding the tax credits taken by ComEd for the power purchased from the CDT landfill at Joliet.

In addition, Staff recommends that the Commission require that the investigation proceed on an expedited basis so that actions regarding State tax credits are undertaken in a timely manner. As such, the Commission should issue a final Order no later than 6 months from the date that the Commission begins this investigation.



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